Industry Canada Industrie Canada

Q4 2011 VENTURE CAPITAL MONITOR

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A QUARTERLY UPDATE ON THE CANADIAN VENTURE CAPITAL INDUSTRY

Canadian high growth innovative small and medium-sized enterprises (SMEs) that commercialize research depend to a large extent on the venture capital (VC) industry for funding. Therefore, a strong VC industry is important for the growth of this segment of SMEs. The goal of this series is to provide current information about the VC industry in Canada. To this end, the series will track trends in investment activity, report on topical VC-related research and look at key technology clusters where VC investment is taking place.

INTRODUCTION

This year-end issue of the Venture Capital Monitor covers venture capital (VC) activity from January 2011 to December 2011, which experienced its highest level of investments in over four years.

VC ACTIVITY OVERVIEW

Investment and fundraising

Increase in year-over-year investment

Canadian VC investment experienced its strongest annual performance since 2007 as $1.51 billion was invested in 504 deals. This represents a 34 percent increase over the $1.13 billion invested during 2010 (Table 1). Per quarter investment levels remained stable throughout the year with $342 million invested over Q4 2011, comparable to the three previous quarters and nearly 40 percent greater than Q4 2010. While overall investment has recovered from the historic lows experienced in 2009 it continues to remain shy of the $2.05 billion invested in 2007 (Figure 1).

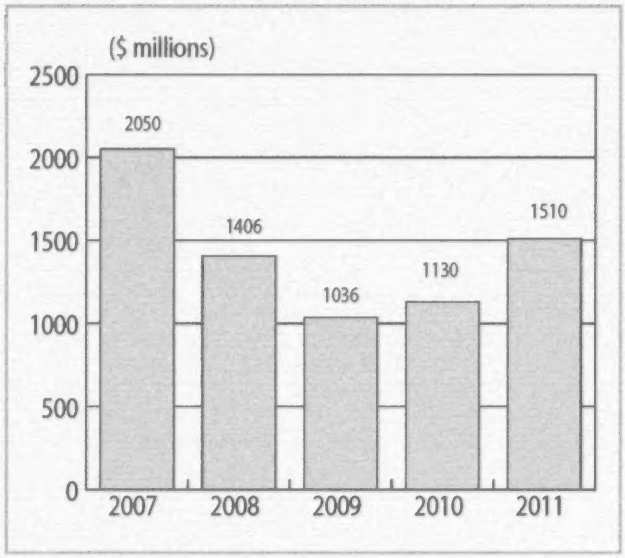
In contrast to improved investment levels, VC fundraising remained relatively unchanged for fiscal year (FY) 2011 as $1.03 billion was raised (Table 1). This is 2 percent more than 2010 and is in line with the six year fundraising average (approximately $1.04 billion). Retail VC funds captured $402 million in 2011, accounting for the largest share of total new commitments, or 39 percent. After leading trends in 2010, private funds, which attracted $368 million last year, accounted for a reduced 36 percent.

Table 1: VC investment and fundraising, FY 2010 and FY 2011

	FY 2010	FY 2011	% Change
	($ billions)		
Investment	1.14*	1.51	34
Fundraising	1.01	1.03	2

* Numbers may not match due to rounding.
Source: Thomson Reuters Canada 2012.

Figure 1: VC Investment by year, 2007 to 2011



Source: Thomson Reuters Canada 2012.

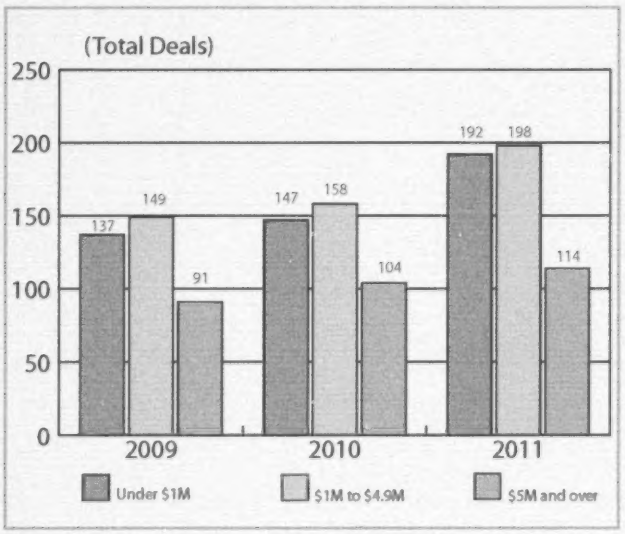
Canada

Deal size

Small increase in year-over-year deal sizes

In 2011, VC investments backed 504 firms, a 23 percent increase over 2010 (Figure 2). This is the highest level of total deals completed since 2005 when 595 firms received VC financing. Despite a substantial increase in the overall value of investments, year-over-year average deal size increased by only 7 percent to $3 million in 2011 as investments were spread over considerably more deals. While total deals completed increased on both the low and high ranges, increases were most substantial in the under $1 million and $1–$4.9 million ranges.

Figure 2: Distribution of VC investment by deal size, 2009 to 2011



Source: Thomson Reuters Canada 2012.

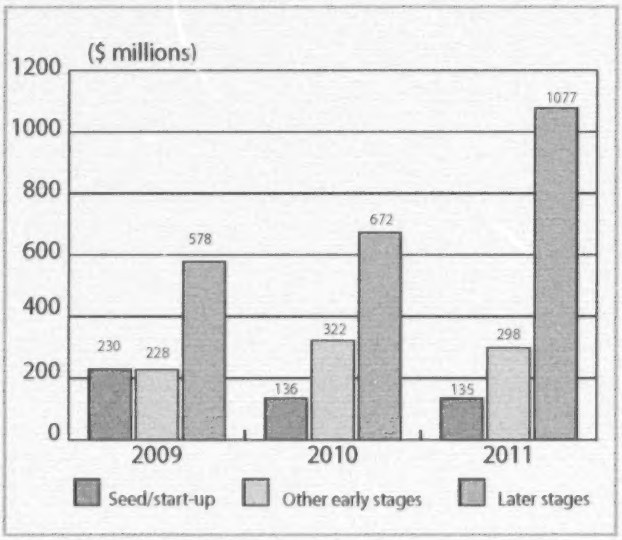
Stage of development

Small decrease in value of seed/ start-up investment but large increase in later-stage investments

Investments were increasingly concentrated in later-stage deals during 2011 attracting approximately 71 percent of all investment dollars. The $1.08 billion invested into later-stage deals in 2011 represented a 60 percent increase over the $672 million invested over 2010 (Figure 3). The 320 completed later-stage deals was the second highest annual figure over the past decade with foreign funds representing 31 percent of total later-stage deal value.

In fact, 2011's increase in total investment levels can be entirely attributed to increased later-stage activity as year-over-year investment levels dropped at all other stages compared to 2010. Deal sizes at the earlier stages fell as $135 million was invested into 113 seed and start-up stage companies in 2011 ($1.1 million/deal) compared to $136 million into 72 companies in 2010 ($1.9 million/deal).

Figure 3: VC investment by stage of development, 2009 to 2011



Source: Thomson Reuters Canada 2012.

New versus follow-on investments

Substantial year-over-year increase in both new and follow-on deals

There were 226 first-time VC deals recorded in 2011, 52 more than during 2010 and the highest figure experienced since 2005. These new deals were worth approximately $407 million, a 14 percent year-over-year increase. New deals at the seed and start-up stages of development experienced notable growth with more than double the amount of seed/start-up deals completed than during 2010. Completed follow-on deals also experienced a substantial increase, mainly at the later-stages as 181 firms attracted follow-on VC during 2011 compared to only 128 during 2010 (Table 2).

Table 2: Number of companies that received new and follow-on investment, 2009 to 2011

Investment		2009 Total	2010 Total	2011 Total
New	Seed/ start-up	48	33	74
	Other early stages	17	24	13
	Later stage	82	117	139
	All	**147**	**174**	**226**
Follow-on	Seed/ start-up	39	39	39
	Other early stages	79	68	58
	Later stage	112	128	181
	All	**230**	**235**	**278**
Total		**377**	**409**	**504**

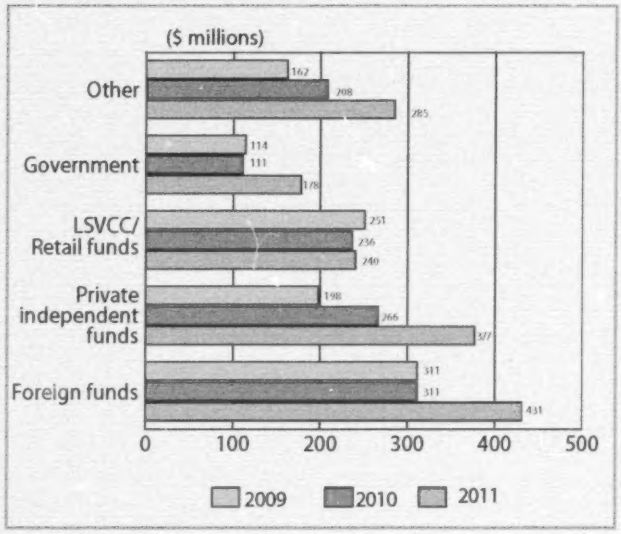
Source: Thomson Reuters Canada 2012.

Type of investor

Increase among all investor types with foreign funds pacing activity during 2011

Virtually all investor types were more active in the market during 2011 than during 2010. For the eighth consecutive year foreign funds were the most active investors in Canadian VC having invested $431 million in 89 deals compared to $311 million in 74 deals over 2010. As a result, cross-border activity accounted for nearly 28 percent of total dollars invested, which is higher than the traditional market share. Private independent funds also experienced a notable increase in activity having invested their highest single year amount since 2001 with $377 million placed into 179 companies. Labour-sponsored venture capital corporations (LSVCC) and retail fund activity remained virtually the same having invested $4 million more in 2011 than during 2010 (Figure 4).

Figure 4: Distribution of VC investment by type of investor, 2009 to 2011



Source: Thomson Reuters Canada 2012.

Fundraising

Fundraising stable as total raised approximates six year trend

New supply raised by Canadian VC funds remained virtually unchanged over the year as $1.03 billion was raised. Fundraising over the year was largely buoyed by a strong second half of the year during which nearly $600 million in new capital was brought into the market. After leading trends in 2010, private independent funds, which attracted $368 million last year, accounted for a reduced 36 percent. Twenty-seven domestic VC funds were responsible for new commitments last year, 11 of which reflected initial or final partnership closings. This compares against 33 funds that were comparably active in 2010. Individual contributions into LSVCCs raised $402 million.

Regional distribution

Increase in VC investment in Quebec and Ontario

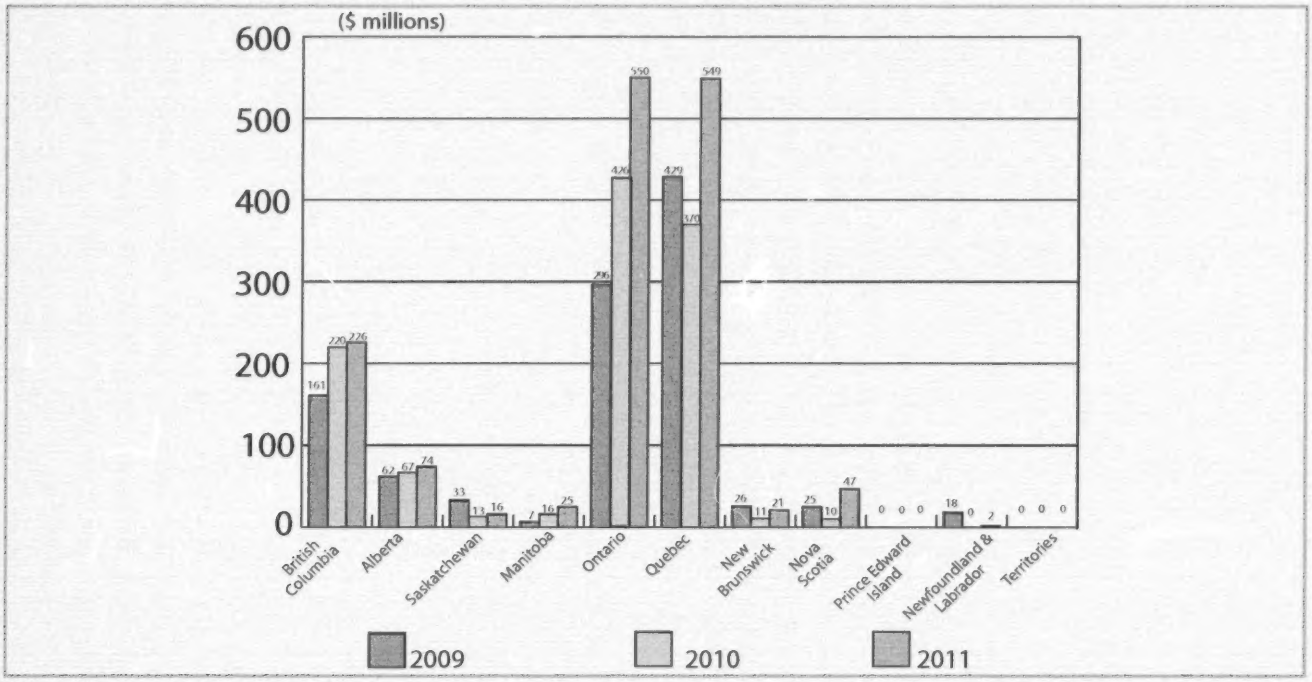
In 2011, the value of VC invested in each of Canada's active provinces increased over 2010. Quebec led Canada in the amount of deals completed (284), accounting for more than half of all completed Canadian deals but Ontario attracted the greatest value of VC ($550 million) (Table 3 and Figure 5). Close to three quarters of all VC investment activity occurred in Quebec and Ontario with the largest increase in investments occurring in Quebec, where companies received 48 percent more in 2011 than in 2010. British Columbia continued its recent strong performance buoyed by high levels of life sciences and environmental technologies investments.

Table 3: Number of companies receiving VC by province, 2010 and 2011

	2010	2011	% Change
British Columbia	52	47	-10
Alberta	22	18	-18
Saskatchewan	5	7	40
Manitoba	8	5	-38
Ontario	117	127	9
Quebec	192	284	48
New Brunswick	7	6	-14
Nova Scotia	6	7	17
Prince Edward Island	0	0	0
Newfoundland & Labrador	0	3	N/A
Territories	0	0	0

Source: Thomson Reuters Canada 2012.

Figure 5: Regional distribution of VC investment in Canada, 2009 to 2011



Source: Thomson Reuters Canada 2012.

Sector distribution

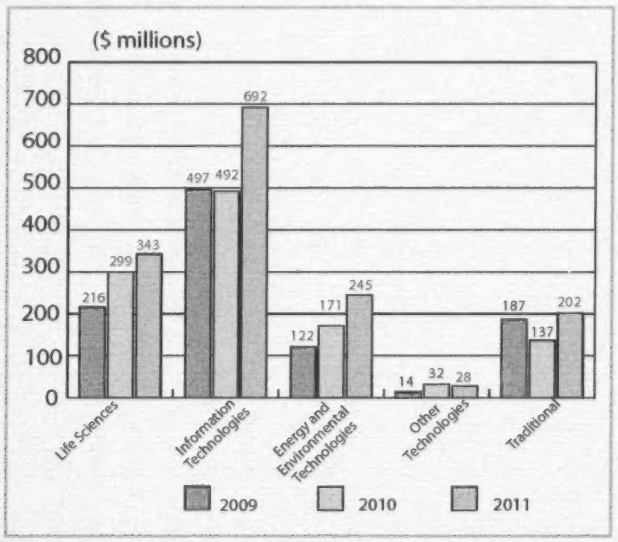
Substantial growth in ICT driven by new investments into software and internet-based companies

Nearly all sectors experienced year-over-year growth in terms of dollars invested in 2011. Investments into information and communication technology (ICT) firms continued to pace financing with $692 million invested into 194 firms, or 46 percent of all VC (Figure 6). This represents a 41 percent increase of the $491 million invested in ICT in 2010. Growth in ICT VC has largely been driven by investments into internet and software companies, growing from $201 million invested to $435 million in just two years.

The $245 million attracted by the energy and environmental technologies sector was the strongest year for the sector on record. This performance was primarily driven by financings into alternative energy companies in Quebec, Ontario and British Columbia as a result of several very large deals. In particular Enerkem Technologies Inc. of Montréal, Quebec closed a $59 million deal in June.

Capital invested in Canadian life sciences firms increased by about 15 percent over 2010. Notably Ontario, Quebec and British Columbia attracted $106 million, $104 million and $93 million respectively.

Figure 6: VC investment by industry sector, 2009 to 2011



Source: Thomson Reuters Canada 2012.

GOVERNMENT ACTIVITIES

Business Development Bank of Canada Activities

The Business Development Bank of Canada (BDC) made seventeen VC commitments totalling $13.0 million during the fourth quarter of 2011. These financings were worth a total of $53.7 million including contributions by co-investors (Table 4). On top of direct financings, the BDC contributed nearly $41 million to three private independent funds in Toronto and Montréal, which had cumulative closings of approximately $350 million.

Table 4: VC activities of the Business Development Bank of Canada, Q4 2011

	BDC	Co-investors	Total	Number of deals
	($ millions)			
Seed/ start-up	2.7	3.1	5.8	2
Development	9.2	34.6	43.8	11
Later stage	1.1	3	4.1	4
Total	**13**	**40.7**	**53.7**	**17**

* Numbers may not add up due to rounding.
Source: Business Development Bank of Canada.

NOTES

This publication is part of a series prepared by the Small Business Branch. The branch analyses the financial marketplace and how trends in this market impact small businesses' access to financing. Current research is focused on high-growth firms, the aspects of both Canada's VC and general business environment that affect the success of these firms, and the key players in the risk-capital market (for example, VC firms and angels).

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ISSN 1911-9267
60996

Aussi offert en français sous le titre *Le Moniteur du capital de risque — Quatrième trimestre de 2011.*